City of Chicago
Committee on Finance
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Dear Ms. Georges and Ms. Lumpkin,

Certain facts regarding the City's contract with Redflex Traffic Systems, Inc. ("Redflex") lead me to believe that the procurement and contracting process followed does not abide by the legal standards to which the City is subject. The contract has had four incarnations, each substantially and materially different enough from each other and the original RFP that their non-competitive execution defies law and logic. This contract is subject to competitive procurement, a fact attested to by the refusal of the City's Sole Source Review Board to approve a justification for non-competitive procurement. The facts and applicable legal framework as I understand them are set forth in additional detail below. As a result, I contend the original contract and subsequent modification awards contravene open and competitive procurement required by law. Finally, it is unfathomable that a contract of this nature and scope does not comply with the City's deeply entrenched commitment to provide full and fair participation of minority and women-owned business enterprises in City projects.

I. HISTORY OF CONTRACTING PROCESS WITH REDFLEX

The chronology and nature of the Redflex contracting process is detailed and rather extensive. In 2003, the City of Chicago ("City") issued a Request for Proposal (RFP) for its Digital Automated Red Light Enforcement Program (DARLEP). The RFP described three phases of the program. The first "testing" phase required short-listed respondents to install one (1) full service red light

enforcement system at a designated intersection. Phase two would require the selected respondent to install equipment in the remaining nineteen (19) intersections upon issuance of a "notice to proceed." Phase three would consist of expansion in the Scope of Services which could "include, but not be limited to, additional intersections and the ability to monitor speed data and other moving violations." The lack of specificity in this provision renders it unenforceable which cannot be relied upon to justify expansions such as have occurred in this case.

In January 2004 a contract presumably pursuant to the RFP, but with substantially different terms, was awarded to Redflex in an amount of $1,940,000. For this amount, the City would purchase at least ten (10) systems during the first year. The contract also granted the City the option to purchase up to twenty (20) systems during each of the first two twelve-month periods following the contract's effective date and during each twelve-month period of any extension option exercised by the City. The contract term was from October 2003 to October 2005 (the RFP also indicated an initial two-year term) with extension options of three additional one-year periods (the RFP indicated two additional one year periods). Thus, the contract can be read as a two-year—possibly five-year—contract with a minimum purchase requirement of ten (10) systems in the first year and the option to purchase up to twenty (20) systems during each of the possible five years, for a possible total of up to one hundred (100) systems. The contract did not grant Redflex the exclusive right to sell monitoring systems to the City nor did it obligate the City to purchase more than ten (10) systems. The City retained authority to procure additional systems from another vendor after having purchased twenty (20) from Redflex. As I understand it, this contract did not provide for funding beyond the minimum required ten (10) systems.

On December 23, 2004, a contract "modification" added $1,080,000 to the contract, increasing its value to $3,020,000. The modification now provided that the City would buy at least twenty (20) systems during the two years following the contract's effective date (as opposed to the ten (10) required in the first contract). The City had the option to purchase additional systems during this period and during each year-long extension of the three that the City could exercise. Pursuant to this amendment, then, the minimum purchase doubled what was in the original contract.

A second contract "modification" awarded on November 23, 2005 added approximately $10.5 million to the contract for a total obligation of approximately $14 million. The scope of services changed to allow for the purchase of fourteen (14) systems in the initial two-year term in addition to the twenty (20) systems that required by the first amendment (for a total of thirty-four (34) systems during the first two years). Additional systems beyond the thirty-four (34) and beyond the first two years could be purchased upon the City's notification to the vendor in writing that it wanted more. This modification also eliminated the one-year extension options and instead increased the contract term by three years (making the term from 2003 through 2008).

In January 2007, a third contract "modification" was awarded. According to the new contract, the City was already operating sixty (60) systems by October 2006. It is unknown whether, when, or how the Department of Procurement identified or secured funding sources for those systems purchased after the thirty-four that were provided for in the second contract

modification. This third modification increased the contract price by $23,500,000 to total $36,949,000 and provides for the purchase of one hundred (100) systems in addition to the sixty already in place. This is total of one hundred sixty (160) systems is one hundred and forty (140) more than the amount contemplated in the RFP (potential expansion provision notwithstanding) and sixty (60) more than the maximum one hundred (100) provided for (but not funded) in the original contract. The technical specifications also changed in the course of the modifications.

The Department of Procurement Services has indicated to my staff that they intend to issue an RFP for additional systems in March 2007.

II. PROCUREMENT PROVISIONS TO WHICH THE CITY IS SUBJECT

Pursuant to statute, the City is required to follow certain procedures when awarding contracts and these are described in the "Municipal Purchasing Act for Cities of 500,000 or More Population" ("Purchasing Act"). Smith v. F.W.D. Corp., 106 Ill. App. 3d 429 (1982). The Purchasing Act requires that all contracts involving amounts in excess of $10,000 shall be let by free and open competitive bidding after advertising to the lowest responsible bidder subject to exceptions discussed below. 65 ILCS 5/8-10 *et seq*. The City increased the threshold amount to $100,000. Mun. Code of Chi., § 2-92-650. Proposals to award contracts shall be advertised in a manner set forth by the Act. Moreover, the advertisement for bids "shall describe the character of the proposed contract or agreement in sufficient detail to enable the bidders thereon to know what their obligations will be...." 65 ILCS 5/8-10-7. A contract executed in violation of the Purchasing Act is null and void as to the municipality and amounts expended may be recovered. 65 ILCS 5/8-10-21. An official who "knowingly and intentionally lets a contract in violation of the competitive bid requirements" forfeits his or her office. Id.

III. THE CONTRACTING PROCESS CONTRAVENED COMPETITIVE BIDDING STANDARDS

It is not apparent to me that the DARLEP project is exempt from the competitive bidding requirement. The Municipal Purchasing Act provides the following exception to the requirement:

> Contracts which by their nature are not adapted to award by competitive bidding, such as but not limited to contracts for the services of individuals possessing a high degree of professional skill where the ability or fitness of the individual plays an important part, contracts for supplies, materials, parts or equipment which are available only from a single source, contracts for printing of finance committee pamphlets, comptroller's estimates, and departmental reports, contracts for the printing or engraving of bonds, water certificates, tax warrants and other evidences of indebtedness, contracts for utility services such as water, light, heat, telephone or telegraph, and contracts for the purchase of magazines, books, periodicals and similar articles of an educational or instructional nature, and the binding of such magazine, books, periodicals, pamphlets, reports and similar articles shall not be subject to the competitive bidding requirements of this Article. 65 ILCS 5/8-10-4.

Establishing and executing a red light enforcement program is not a project that fits within any of these exceptions. Therefore, it remains subject to open and competitive bidding standards

regardless of whether the City initiated this procurement process with a solicitation of bids or a solicitation of proposals.

Based on the understanding that the Redflex matter was subject to competitive procurement, the analysis that follows describes key elements of open and competitive bidding and how the facts presented in this matter have compromised them.

The purposes of requiring governmental units to engage in competitive bidding are to "invite competition, to guard against favoritism, improvidence, extravagance, fraud and corruption, and to secure the best work or supplies at the lowest price practicable." Smith v. F. W. D. Corp. (1982), 106 Ill. App. 3d 429 (1982) (quoting 10 McQuillin, Municipal Corporations § 29.29, at 302 (3rd ed. 1981)). The purpose is also to ensure that all potentially interested persons are motivated to bid by the assurance that they will have the opportunity to do so fairly and intelligently. Illinois Jurisprudence, Municipal Law §14:27 (2007).

Differences between the RFP and ensuing contracts with Redflex constitute material variances that are inconsistent with competitive bidding requirements. An Illinois court has found that where there was a "material variance" between an RFP's requirements and an ensuing contract's terms, the contract was entered into without competitive bidding and was therefore invalid. Smith v. Intergovernmental Solid Waste Disposal Association (ISWDA), 239 Ill. App. 3d 123 (1992). The test of whether a variance is material is whether it gives a bidder a substantial advantage or benefit not enjoyed by other bidders. Id. Similarly, the U.S. Supreme Court has found that a contract was properly abrogated where the final contract was materially variant from the specifications of the contract as it was advertised. U.S. v. Ellicott, 223 U.S. 524 (1911). In that case, the Court found that where the contract was required to be let only after competitive bidding, the contracting body had no authority, without re-advertising, to enter into a contract for barges of a radically different type from those originally specified. Id. The Illinois Supreme Court has found a contract that had to be competitively awarded void when it was expanded to include work not mentioned in the advertisement. Littler v. Jayne, 124 Ill. 123 (1888). This, the Court found, amounted to an invalid "private contract" made between the parties. Id.

Comparing the facts and rationale set forth in Smith v. ISWDA with the process followed in the instant matter shows that the differences between the RFP at issue here and the resultant Redflex contracts are sufficiently material as to not be in keeping with competitive bidding standards. In Smith v. ISWDA, garbage haulers in Champaign County filed a complaint against ISWDA regarding a contract to design, construct, and operate a material recovery and transfer facility. They argued that the contract was entered into without competitive bidding. The trial court agreed, finding that there were a number of variations between the requirements in the RFP, the winning bid, and the winning bidder's obligations under the contract. Id. at 131. It considered whether there was a "material variance" between what the RFP required and what the resulting contract contained. Id. at 142. "The test of whether a variance is material is whether it gives a bidder a substantial advantage or benefit not enjoyed by other bidders." Id. The trial court in that case determined that changing the RFP requirements upon entering into the contract makes it difficult to guess who may have been the lowest responsible bidder had the requirements been different and underscores the need that there be no material variances between the contract and the request for bids. Id. at 143. It observed that "[w]hen material changes are made, after the

bids are submitted, the public body no longer knows who the lowest bidder would have been...had accurate specifications and details been provided to the contractors." Id.

Contract price was deemed to be the most important variance in the Smith case. After selecting the bid, the successful bidder, XL, was allowed to raise the contract price by $1.48 million. The trial court stated: "if this is not a material variance then nothing is." Responding to the ISWDA's assertion "that the 'modification' in XL's price occurred after it was selected," the trial court observed that "this practice, if permitted, leads directly to the problems that competitive bidding is meant to prevent." In affirming the trial court, the decision cites a New York case, stating that "the heart of this process must be public competition, not private negotiation." Id. at 668.

Regarding the Redflex matter, the differences between the RFP, the original contract, and subsequent modifications are substantial and have given Redflex an advantage not enjoyed by other bidders, thereby rendering those differences "material variances" that contravene competitive bidding requirements. As in Smith, the RFP specifications differed from the first contract's terms which, in turn, came to differ greatly from those in the subsequent modifications. Also like the case in Smith, the contract price changed drastically from one modification to the next. The detriment to other bidders is two-fold. First, the red light project that bidders were initially asked to bid for was not what was implemented in the end. They may have bid differently if the RFP was not primarily held out as one for a pilot project with a possibility of expansion and instead was one that made the likelihood and plan for expansion more definite. Second, by retaining Redflex beyond the pilot program period without reopening the procurement process, the City's DARLEP system became enmeshed with Redflex systems which the Department of Procurement has indicated are incompatible with those of other possible vendors. As a result, all amounts expended to date would result in a loss to the City were it to select another vendor at this point. Therefore, the differences among the RFP and subsequent contracts gave Redflex an advantage that other bidders did not have, rendering them "material variances" at odds with open and competitive bidding requirements.

I understand that it may be argued that there was no "material variance" between the RFP and ensuing contracts because the original RFP contained a project expansion provision. This, however, brings to light another factor used to determine whether competitive bidding exists—whether the terms and specifications set forth have the appropriate degree of detail. An Illinois appellate court has found that that "the nature of the work required should be stated as definitely as is practicable...[i]t is the duty of public officials, in advance of calling for bids, to adopt reasonably definite plans or specifications." Smith v. F.W.D. Corp., 106 Ill. App. 3d 429 (1982). Noting that very detailed specifications can also be used to limit potential suppliers, the court concluded that "a proper balance must be struck between detail and generality." Id.

Although the RFP in this case contained an expansion provision, it does not adequately portray the scope of the project as it came to be. First, it simply stated that an expansion in the Scope of Services "can include, but not be limited to, additional intersections and the ability to monitor speed data and other moving violations." This provides no guideline as to how many additional intersections are foreseen or whether additional systems will necessarily be a part of the expansion of services. Second, given that the RFP specifically delineates a pilot program and only generally addresses expansion, it is not reasonable to surmise that this also serves as an RFP

for a city-wide implementation of the program. That the RFP contemplates utilizing additional vendors makes it even less presumable to potential bidders that a successful bid would translate into an exclusive contract to implement a large scale red light enforcement program.

Another argument that may be made in favor of the validity of the Redflex contract modifications is that these were just that—amendments that did not change the rights or obligations of the parties and cannot therefore be considered "new" contracts that must be re-let for competitive bidding. Under Illinois law, "the modifications must effect a material alteration of the parties' rights and obligations before it can be said that the parties intended a new contract or agreement." McKay Nissan, Ltd. v. Nissan Motor Corp., 764 F. Supp. 1318, 1319 (D. Ill. 1991) (referencing Bitronics Sales Co. v. Microsemiconductor Corp., 610 F. Supp. 550, 557 (D. Minn. 1985); Easterby-Thackston, Inc. v. Chrysler Corp., 477 F. Supp. 954, 956 (D.S.C. 1979)). The court in McKay Nissan, determined that the amendments that neither changed the parties' contractual rights nor varied the responsibilities and duties of either party were contractual modifications that were too insubstantial to have established a new contract that replaced the original agreement. Id. at 1320.

In this case, it appears that the parties intended a "material alteration" of rights and obligations and that the modifications are not simply incidental to the original contract. From RFP to contract to modifications, the City's obligations and Redflex's equipment and support obligations changed dramatically. In fact, documentation offered in support of earlier attempts to make this a sole source contract refers to the proposed project expansion as a "new contract" and sets forth obligations and goals that significantly exceed the scope of the original contract. The terms in the contract in its present form cannot be reconciled and read together with those in the first contract. Therefore, it is reasonable to conclude that the parties intended to supersede the original contractual agreement. As such, the "modifications" were in fact new contracts that could only have been let by free and open competitive procurement methods.

On at least one occasion, it has been represented to my staff that the City had simply been exercising its options under the contract when ordering new systems and, admittedly, a special consideration arises when the contract at issue is an "option" contract, as this one may have been in its first embodiment. "The law of the Federal Circuit is clear that the exercise of an option only gives rise to a new contract when the option, itself, is the principle [*sic*] subject of the underlying contract, i.e., an 'option contract.'" Fluor Enterprises v. United States, 64 Fed. Cl. 461, 487 (Ct. Cl. 2005). "Obligations arising from the exercise of an option are part of a new contract only when the option was the principal subject matter of the bargain. That rule has consistently been applied to government contracts." Id. Options in government contracts generally create extensions of the obligations of the original contract rather than new, independent obligations. Id. An option contract is an agreement in which the buyer has the right (not obligation) to exercise by buying or selling an asset at a set price before a future date and the seller has an obligation to honor those contract terms.

Although the Redflex contract might arguably have been considered an option contract, at least in part, it was no longer so after the second modification. Moreover, the City never exercised those options. They were eliminated in 2005, just when the City would have been able to exercise them. Therefore, that the Redflex contract might once have been considered an option

contract does not now mean that the modifications were the mere exercise of an option that did not create a new contract.

In sum, the three contract modifications were not mere amendments within the scope of the original contract. As such, a new contract or agreement emerged and should therefore have been competitively bid.

IV. CONCLUSION

The differences between the scope of the project delineated in the RFP and the scope formed by the subsequent contracts mean that the required competitive bidding process was compromised in the City's dealings with Redflex. An RFP for a pilot project initially valued at $1.9 million with an exceedingly vague and therefore unenforceable provision as to expansion cannot be considered the same as an RFP for a project that has come to be valued at nearly $40 million.

As indicated above, the existing contract with Redflex should be declared null, void, and non-binding upon the City. In light of the foregoing, I urge the rescission of the January 2007 contract must be rescinded and that efforts to purchase additional systems be abandoned until an open and competitive procurement process is undertaken.

The Sole Source Review Board consists of public officials who are well versed in what constitutes a transparent and competitive purchasing and procurement process. Their assessment that the project at stake here did not lend itself to non-competitive procurement should not be disregarded. Moreover, we are all entrusted to ensure that this process is inclusive, particularly of minority and women-owned business enterprises. That the Redflex contract negotiations fail on all of these accounts is unacceptable.

Very truly yours,

Edward M. Burke